

BEFORE THE
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY
DOCKET NO. D.T.E. 98-32

INITIAL COMMENTS OF TENNESSEE GAS PIPELINE COMPANY

Pursuant to the Notice of Inquiry issued by the Massachusetts Department of Telecommunications and Energy ("DTE") on April 3, 1998, Tennessee Gas Pipeline Company ("Tennessee") hereby submits its Initial Comments in the captioned proceeding.

**I.
INTRODUCTION**

Tennessee owns and operates an extensive interstate natural gas pipeline system which extends from the Gulf Coast to New England. In addition, Tennessee's transmission system interconnects with the pipeline system of TransCanada Pipelines Limited at the U.S.-Canada border near Niagara Falls, New York.

Tennessee is one of the interstate natural gas pipelines which directly serve Massachusetts and provides transportation and storage services to a majority of the local distribution companies ("LDCs") and municipal gas companies in Massachusetts. Tennessee's extensive transmission system provides consumers with access to Gulf Coast, Mid-Continent and Canadian gas supplies.

Tennessee supports the framework which the DTE has established to effectuate the unbundling of the retail natural gas industry in the Commonwealth of Massachusetts. As an initial matter, Tennessee submits that in order for the efficiencies of the market to be fully realized, retail unbundling programs must not inhibit competition. Rather, each segment of the natural gas industry must be allowed to compete based on its own merits. Further, each LDC should coordinate with its interconnecting pipeline(s) regarding operational, tariff and contract issues in order to assure that (1) the transition to a fully unbundled market will be smooth, and (2) end users will be provided with reliable service. Tennessee intends to continue meeting the market requirements for natural gas service in Massachusetts in the most economical and efficient manner.

Tennessee will herein respond to those questions contained in the DTE's request for information which directly impact its role as an interstate pipeline serving markets in Massachusetts. Specifically, Tennessee will respond to Question Nos. 2, 4, 6 and 11. In addition, Tennessee welcomes the opportunity to clarify its comments and/or provide additional information at the hearing scheduled by the DTE.

II.

CAPACITY ASSIGNMENT PRINCIPLES

(INFORMATION REQUEST NO. 2)

One of the most difficult issues facing the DTE is how the upstream transportation and storage capacity currently held by LDCs should be made available to marketers. The DTE has been presented with two alternative capacity disposition mechanisms: (1) mandatory capacity assignment, whereby marketers are required to take the LDC's capacity; and (2) a voluntary capacity assumption program, whereby marketers are entitled, but are not obligated, to take the LDC's capacity.

Tennessee recognizes that there are pros and cons associated with voluntary capacity assignment, mandatory capacity assignment and the portfolio auction. Tennessee anticipates that these issues will be adequately addressed by those market participants most directly involved in the assignment of capacity. Tennessee is willing to accept whichever of these capacity assignment schemes is adopted by the DTE and which is consistent with Tennessee's tariff. Tennessee is committed to serving the future natural gas needs of customers in the Commonwealth of Massachusetts. However, because Tennessee is the lowest cost provider of transportation service to markets in the Commonwealth of Massachusetts and the majority of its firm transportation service agreements expire on November 1, 2000, Tennessee's preference is for voluntary capacity assumption. Tennessee also believes that natural gas consumers or their agents should have access to the pipeline supplier of their choice. The unbundling process should not skew the decisions that rational market participants would otherwise make. Tennessee recognizes that a voluntary approach creates the potential for stranded costs as customers migrate from bundled sales to unbundled transportation service. However, stranded costs will be incurred in the transition to a competitive market which ultimately will benefit all natural gas consumers. If the DTE were to adopt a voluntary approach to capacity assignment, a satisfactory mechanism would have to be developed to assure the recovery of stranded costs.

Whichever method of capacity assignment is adopted by the DTE, it is appropriate for the DTE to establish a definitive unbundling schedule. This will enable LDCs to plan for their future role and provide all parties with advance notice of the framework required for planning. Assuming an implementation date of November 1, 1998, a transition period should not last longer than three or four years. A transition period is necessary so that the DTE and the market participants can see how the unbundling process unfolds before making permanent decisions. The natural gas market in New England likely will undergo significant changes in the next few years. In particular, increased Canadian gas supplies will be delivered into the region, and natural gas will be used to supply a growing power generation load. These changes could have unforeseeable impacts. The DTE must assure that the comprehensive permanent unbundling program which it adopts takes into account these (and any other) changes in the market. Several years of actual experience with unbundling will be more valuable in developing a permanent unbundling scheme than one year of debate.

Whether the DTE adopts a voluntary or a mandatory capacity assignment scheme, there are other issues which need to be resolved to assure a smooth transition to an unbundled retail market. These issues are discussed below.

III.

RELIABILITY OF UNBUNDLED SERVICE **(INFORMATION REQUEST NO. 4)**

One of the major challenges facing the DTE is to ensure that there will not be any decline in the reliability of retail service after unbundling. In reviewing the Status Report on the Massachusetts Gas Unbundling Collaborative (“Status Report”), Tennessee has paid particular attention to reliability of service issues. For example, the Status Report does not appear to discuss the implementation of measures or checks and balances which will preclude marketers which take permanent assignment of LDCs’ upstream transportation contracts from amending such contracts to change the primary delivery point(s) thereunder to some point(s) other than the LDC’s city-gate delivery meter(s). If the LDC does not retain the contract rights on the assigned capacity, a marketer would have the ability to amend the transportation contract to delete the LDC’s city-gate as a delivery point and, instead, add an alternative primary delivery point. Tennessee is under no obligation to deliver gas to an LDC’s city-gate unless there is a transportation agreement in place providing for such primary deliveries. Further, once a shipper amends the primary delivery point(s) under its service agreement, capacity at the original delivery point may not be available if the shipper seeks to amend back to such delivery point at a later date.

IV.

RESPONSIBILITY FOR RELIABLE AND ADEQUATE SERVICE **(INFORMATION REQUEST NO. 6)**

The DTE has requested that parties address issues regarding the responsibility of LDCs and marketers for assuring reliable and adequate service to all end users during the transition to fully unbundled service. Tennessee’s comments will address the following three issues: (1) LDCs’ ability to hold upstream capacity; (2) LDCs’ exercise of roll-over rights under transportation contracts which will expire during the transition period; and (3) the maintenance of operational balancing agreements (“OBAs”) at city-gate delivery points.

A critical component of any unbundling program must be the preservation of reliable and adequate service. However, an unfortunate reality of competition is the failure of certain market participants. Thus, a structure must be implemented to ensure that system reliability is maintained in the event a third-party provider fails to perform its service obligations for any reason. Moreover, LDCs should continue to review the gas supply needs of new and existing customers through the transition period. LDCs should be permitted to hold upstream capacity in their own name -- during the transition period and afterwards -- in order to respond to emergencies, maintain the operational integrity of their systems, serve growth markets behind the city-gate and/or render a merchant service.

The DTE also needs to establish guidelines to govern recontracting decisions which will have to be made during the transition period. In that regard, the majority of Tennessee's firm transportation agreements with Massachusetts LDCs expire on November 1, 2000. However, by November 1, 1999, these LDCs must notify Tennessee whether they will terminate their service agreements or extend the terms of such agreements. If an LDC fails to notify Tennessee of its decision by November 1, 1999, the LDC's service agreement will automatically roll-over for a five-year term. Under Section 10.5 of the General Terms and Conditions of Tennessee's tariff, a firm shipper who was a party to the Stipulation and Agreement in Docket Nos. RP93-151, et al. (referred to hereinafter as the "Original Customer") and who elects to extend its service agreement(s), may extend such service agreement(s) for a term of less than or equal to five years ("Primary Extended Term") and may elect a transportation quantity up to the maximum daily quantity specified in its service agreement(s). The Original Customer has the same right to roll-over its service agreement(s) at the end of the Primary Extended Term for a Secondary Extended Term. Pursuant to Section 10.5(c), the Original Customer has the right, prior to the expiration of the Second Extended Term, either to terminate its agreement(s) or extend the term of the agreement(s). If, at that time, the shipper elects to extend the agreement(s), the extension is governed by Section 10.4 of the General Terms and Condition of Tennessee's tariff. Under Section 10.4, if a shipper elects to extend its agreement(s), or any portion of its contract quantity for less than the five-year automatic extension period, then Tennessee has the option either to accept the shipper's requested extension or require the shipper to exercise its right of first refusal after Tennessee holds an open season. Under these procedures, the existing shipper must match the highest net present value bid for its capacity in order to retain such capacity.¹

As the foregoing discussion suggests, LDCs will have to make critical decisions during the transition period regarding the status of their firm service agreements with Tennessee. Any decision not to roll-over a contract or portion thereof means that such relinquished capacity becomes generally available capacity and, as such, is available to all other shippers on Tennessee's system pursuant to the NPV open season provisions of Tennessee's tariff. The LDC no longer will have an entitlement to such relinquished capacity. The unbundling process will still be in an infant stage when LDCs have to decide whether to roll-over their contracts. Tennessee submits that LDCs are in the best position to determine the present and future capacity needs of customers behind their city-gates. Under these circumstances, Tennessee submits that LDCs should have the ability to make all recontracting decisions during the transition phase.

Finally, Tennessee submits that there should be only one OBA at each city-gate delivery point, and the OBA should be between Tennessee and the city-gate operator (which is currently the LDC). This is necessary to assure adequate control and an efficient method of balancing flowing volumes at the delivery point. Changing

¹ If, as a result of the open season, Tennessee does not receive an acceptable bid for the capacity, then the shipper may continue to receive service at the maximum rate for the term chosen by the shipper or at any other rate and/or term to which Tennessee agrees.

Tennessee's existing delivery point OBA scheme (1) will increase the administrative burden on all parties at the delivery point, and (2) could jeopardize the reliability of service for customers served by such delivery point.

V.
PIPELINE CONTRACT INFORMATION
(INFORMATION REQUEST NO. 11)

Attached hereto in Appendix A is a list of non-LDC firm shippers on Tennessee which hold capacity rights to delivery points in Massachusetts and the rest of New England. In addition, there are over 600 interruptible transportation ("IT") agreements on the Tennessee system. Because every IT agreement permits deliveries anywhere on Tennessee's system (subject to capacity availability), there is no need for Tennessee to identify its IT shippers in Appendix A.

VI.
CONCLUSION

Tennessee supports the DTE's efforts to unbundle the retail natural gas industry in Massachusetts. The DTE must assure that the unbundling process will enable all potential suppliers to compete on a level playing field in order to fully realize the benefits of competition. Market efficiencies and the benefits of unbundling can be fully realized only to the extent that each segment of the natural gas industry is allowed to compete based on its own merits. Further, the DTE must take all necessary steps to assure reliable service during the transition period and afterwards. Tennessee submits that adoption of an unbundling program consistent with the discussion herein will help bring the full benefits of unbundling to consumers in Massachusetts.

Respectfully submitted,

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